

**KEY LONGTERM DEVELOPMENT ISSUES IN
TUNISIA**

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KEY LONG TERM DEVELOPMENT ISSUES IN TUNISIA*

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Abstract

Two opposite views can emerge when analyzing the Tunisian development experience. The first is a view of success and achievements, and the second is a view of a country facing many weaknesses and challenges. The purpose of this paper is to analyze the strategic factors regarding the development of Tunisia in the long run and to make an assessment of the needed reforms. After a structural adjustment period Tunisia has adhered to the Uruguay Agreements and accepted to belong to a Free Trade Area with the European Union (EU). Do these agreements bring new opportunities or more threats to its fragile agricultural and industrial activities? We will argue that the answer will depend on: 1) the true willingness to adjust hence to accept the negative reactions and the costs generated by reforms, and 2) the ability to create the appropriate conditions for growth and to take advantage of dynamic effects. As to static effects, both the Uruguay and the FTA agreements do not seem in favor of Tunisia. Thus, additional actions are necessary mainly regarding more openness towards countries outside the EU.

ملخص

عند تحليل التجربة التونسية تظهر صورتان متضادتان: الأولى صورة نجاح وانجازات، والثانية صورة دولة تواجه الكثير من نقاط الضعف والتحديات. وتهدف هذه الورقة إلى تحليل العوامل الاستراتيجية المتعلقة بالتنمية في تونس في الأجل الطويل، وتقييم الإصلاحات الضرورية. ذلك أنه بعد مرحلة من الإصلاح الهيكلي، التزمت تونس باتفاقيات أورو جواي وقبلت الإنتماء إلى منطقة تجارة حرة مع الإتحاد الأوروبي. فهل ستوفر هذه الإتفاقيات فرصاً جديدة لتونس، أم أنها ستجلب المزيد من المخاطر على أنشطتها الزراعية والصناعية الضعيفة؟ وسنذهب هنا إلى أن الاجابة تتوقف على الآتي: (١) الاستعداد الحقيقي للإصلاح، وبالتالي لتقبل ردود الفعل السلبية والتكاليف الناجمة عن الإصلاحات، و (٢) القدرة على خلق الظروف المواتية للنمو واستغلال الآثار الديناميكية. أما عن الآثار الاستاتيكية، فإن كلاً من اتفاقيات أورو جواي ومنطقة التجارة الحرة لا تبدو في صالح تونس. لذا، فإن الأمر يتطلب إجراءات اضافية، خاصة فيما يتعلق بانفتاح أكبر على دول هي خارج الإتحاد الأوروبي.

I - INTRODUCTION

Two opposite views can emerge when analyzing the Tunisian development experience. The first is a view of success and high performances and the second is a view of a country having to deal with a lot of challenges and weaknesses in the way of sustainable growth.

Undoubtedly, during the last decades, since its independence (1956), Tunisia has achieved a lot of progress and growth. It was also able to implement ambitious reforms, especially when signs of unsustainability appeared, in the sixties and later in the mid-eighties. Today, it has to undertake deeper reforms in order to reach an even higher level of development. A more systematic modernization process and more appropriate policy choices are necessary, otherwise even regress would not be ruled out.

The purpose of this paper is to analyze the factors that are strategic for the development of Tunisia in the long run. However, since the long run cannot be totally separated from short term policy choices, some attention ought to be paid to the link between recent and short term performances and possible future outcomes. The emphasis will however be put on the key strategic choices, mainly those regarding international relations and industrial policy. The ratification of the free trade Agreement (FTA) with the European Union (EU) is among the most important steps. Is it going to widely open for Tunisia the doors of the prosperous European market including modern technology and investments? Or is it going to be a threat to the fragile industries and agricultural activities that constitute the major part of its productive base? The economy has to become more robust and much more efficient. What is then to be done, given this new and more demanding environment?

Before answering such a question, the first section will deal with the link between the past and the future and will give some insight and assessment of the potential for economic development and the willingness of Tunisia to adjust, that is to accept the sacrifice and the efforts that are required for progress. The second and third sections of the paper will be devoted first to the static and dynamic effects of the international agreements and of the liberalization process, second to the conditions of sustainable growth.

II- THE WILLINGNESS TO ADJUST

Information about past performances and the behavior of the main economic partners are significant for the identification and analysis of long term issues. In particular, they allow one to assess the willingness to undertake the needed adjustments and face the various negative reactions that characterize any reform period.

The results achieved in Tunisia leave room for an optimistic prediction but doubts are also important.

1- The Optimistic View

Optimistically, we can assert that, at least to a certain extent, the country's institutions and decision making mechanisms and the skills it already has allow for a smooth transition and integration within the new international environment.

Among the success indicators, it is meaningful to note that per capita income has grown at an average rate of 3%, during more than three decades reaching, in 1995, a level which is five times the 1960 level, approximately \$ US 18000 a year

During the same period, life expectancy has increased sharply from 50 to 69 years, child mortality decreased, approximately, from 150% to 43%.

In the field of education the number of schools and of students are incomparably higher today. Universal primary education enrollment, for boys and girls, is a fact and illiteracy has been largely reduced (35% in 1994 instead of 80% in 1960).

Income distribution is relatively equitable (the Gini coefficient is nearly equal to the United Kingdom's 0.42). And an important middle class has actually emerged; it constitutes a reserve of skilled labor and under utilized entrepreneurship. It also includes a capable and often dedicated class of managers, both in the public and private sectors. All of these skills are to a large extent the outcome of public schooling and public health facilities and programs.

This accumulation of human capital is obviously a major asset and a source of growth. It also means a substantial capacity to face challenges and to design and implement new plans. In other words, it means that Tunisia will be able to find its way. This point of view is partly supported by the outcomes of the stabilization and adjustment programs, adopted since 1987 and following the foreign payments deficit observed mainly in 1985-86. The implementation of these programs allowed the country to absorb, with a relative ease, the shocks and sacrifices imposed on it inspite of the external and exogenous disturbances that occurred, such as the Gulf war and the severe drought. It was possible to undertake successfully a comprehensive stabilization program including the restriction of consumption, investments, and the limitation of public expenditures and employment and the administration of a sharp depreciation of the Tunisian dinar.

Moreover, structural reforms aiming at the establishment of an open export oriented economy had been implemented and some actions are still under way. They involve not only institutional transformation but also the management of conflicting interests and of social discontent. It is a liberalization process covering, as usual, international trade,

pricing, investment regulation, the financial market, the tax system and other major targets.

The outcome of the stabilization and adjustment programs was a balance of payment recovery, a fast growth of exports (around 10%), and a high enough GDP growth rate (around 4.5%) even in periods of severe conditions.

2 - The Negative Signs

However, there are also negative signs. Liberalization was met by resistance from groups that are threatened with losses. Industries that used to be very protected put pressure to delay tariff reduction and most of all the removal of quantitative restrictions. The government itself had to take into account risks such as the fall in fiscal revenues and social unrest linked to the loss of jobs (World Bank 94).

The long tradition of price control and of imperfect competition in various markets makes price liberalization less effective.

Reforms have been slow indeed in many fields with respect to trade liberalization, privatization and financial policies. Although the strategic options in favor of a market based and outward oriented economy does not seem seriously questioned, the situation is somehow ambiguous and attitudes are sometimes equivocal.

For example, in the fields of international trade, including foreign payments, and regarding financial and capital markets, many reforms are delayed, some policy issues are not yet completely settled and some serious problems are far from being solved; these may even constitute major issues, for Tunisia, in the years to come. (Lahouel 1995 describes a wide range of examples in this regard.)

The contradiction between intended actions and implementation reveals the existence of powerful pressure groups attempting to protect their interests. The point here is not to question interests but to emphasize the long run consequences of the concessions generated by this pressure. The speed and the extent of the reform process convey messages to economic actors and have an important impact on their expectations and therefore on their choices. This is crucial in particular for investors.

Undoubtedly reform management is a hard and risky task and it happens that governments prefer, for short run considerations and because of political and social constraints, not to reveal the intended plan of action, nevertheless, the cost of the induced side effects may be too high.

Too much caution and too many concessions, made in order to avoid confrontation, produce blurred signals and distorted expectations. Investors, for example, may then

delay their actions or misallocate resources. In Tunisia, for example, too much investment is being concentrated in tourism and not enough in manufacturing.

The speed and sequencing of reforms themselves should therefore be more adequately planned and the strategic objectives should always be unambiguously stated and targeted.

II. GROWTH CONDITIONS AND CHALLENGES

Of course, the timing of the reforms and political economic issues may become minor if the planned reforms were not appropriate and the conditions for sustainable growth were not fulfilled.

1 - The Challenge

Tunisia made the commitment to liberalize its economy and become more market and export oriented since the first structural adjustment program it accepted in 1987 and later when it approved the Uruguay Round Agreement and the Free Trade Area (FTA) accord with the European Union, as part of a future scheme covering most of the Euro-Mediterranean region. Consequently, Tunisia has to abide by the World Trade Organization (WTO) rules, to gradually dismantle its trade barriers and to adjust to the abolition of the Multifiber arrangements.

It is to be noted, however, that Tunisia already had free access to most of the EU markets, except for agricultural commodities, which means that the Free Trade Agreement will basically lead to a unilateral elimination of trade barriers on the Tunisian side. Tunisia will have to grant free entry to all EU commodities, while it is not clear yet whether the Tunisian agricultural exports to the EU will ever be less restricted. So far Mediterranean agricultural products such as olive oil, citrus products, vegetables, wines are highly regulated under the Common Agricultural Policy (CAP).

As to the Multifiber Arrangements, they used to protect countries like Tunisia from the much more competitive Asian and other newly emerging countries. Textiles represent a major export for Tunisia, mostly to the EU. Although the latter imposes quantitative restrictions on its textile imports the quotas that are assigned to Tunisia have not been restrictive. In other words Tunisia has practically free access to the EU for textiles and not much gain is to be expected from the FTA in terms of trade opportunities. In fact, it will have to face much stronger competition from countries like China, India, and Pakistan.

It will indeed have to face major challenges. Net losses are not excluded in most calculations, unless dynamic effects are taken into account.

2 - Static and Dynamic Effects of Trade Liberalization

a - Static Effects

From a static point of view, Tunisia will hardly expect any gain. A large chunk of its agriculture and industry will simply be facing sharp competition from higher quality products from more efficient European and Asian rivals. Calculations (Boudhief 1995), (CEPEX 1994) tend to confirm that the net effects on trade flows will be detrimental for Tunisia and will cause job and welfare losses. The diversion effects will be too strong.

This is a serious threat given that capital has been concentrated in a few vulnerable activities, the most vulnerable being those created and developed in a sheltered environment during the seventies. The degree of protection remains indeed quite high (Lahouel 1995) and, technologically, Tunisian industries remain very simple, requiring limited skills and yielding small value added. That is why Asian, and Central and East European countries, where skills are higher and/or wage cost lower, may dominate and leave little room in the market where Tunisia operates.

The diversification issue is serious. Even when compared to other countries of the region, Tunisian exports are undiversified, most of them are traditional and declining, while too much is concentrated in textiles, garments and leather as far as manufacturing is concerned. Tourism, the major service activity, is also fragile and too sensitive to political shocks. As to exports of natural resources, petroleum is vanishing, phosphate is fluctuating and rarely profitable and agriculture is strongly contingent on climate. Hence, potential growth is mainly in manufacturing (table 2).

Consequently, the negative effects should be dealt with mainly through the simultaneous reduction of tariffs towards other important trade partners and through the diversification of its manufacturing capacities. The diversification and development of new and profitable activities constitute an important issue, but static analysis cannot give a satisfactory answer to all the issues involved.

b- Dynamic Effects and Strategic Actions

Dynamic effects should be more substantial than static effects but are harder to evaluate and to identify. In fact, they are not automatic effects. Liberalization is not going to mechanically create the incentive to climb the technical progress ladder, to diversify production and exports and to reach higher quality and value added. Tunisian industrial goods had free entry to the UE and USA markets for a long time and yet not enough happened.

In fact this situation is not so paradoxical. A closer observation of the production network and of the incentive scheme show that some prerequisites are not yet fully

available. The main sources of growth which are closely linked to the dynamic effects are problematic.

We mean by dynamic effects the transformation and widening of production possibility sets generated by externalities and by the ability to benefit from economies of scale. Externalities and economies of scale are organically linked to human capital accumulation, (i.e. education, learning, research) , to innovations, to the efficient provision of services, especially in the field of communication and information, and to the qualities of infrastructure and institutions (Grossman and Helpman 1992). All of these factors are fundamental to achieving competitiveness yet, in the case of Tunisia, a lot remains to be done regarding most of them. Firms are often too small and seldom used to innovative practices and international marketing. They often lack the skilled labor and prefer to operate with the simplest techniques. This is a stylized but accurate enough picture of the typical industrial firm. Outside the firm, the low quality of services and infrastructure cause a lot to yield high transaction costs.

Therefore, if Tunisia is to achieve success within the international market (and there is no alternative), it has to lower its transaction costs and to plan for excellence and high quality.

But such a challenge requires not only time but also massive investments, particularly in public goods and infrastructure. Most of all, profound reforms regarding institutions and incentives are required.

Excellence should become the target, average performances may not allow survival anymore, especially in the industrial sector. Just in order to avoid regress, Tunisia ought to reach much higher quality (World Bank 1994) and performance.

Such a transition puts the analysis again in the dynamic field. Let us look more closely at some of the above evoked factors which are essential for long term development: education, infrastructure, institutions...

Education :

Tunisia has achieved a great deal of progress in the educational field and more generally in the field of human capital development, as indicated above. However, the outcome is rather average (Nemat 1994), if we judge by the rate of enrollment in secondary and higher education, the rate of illiteracy or the type of skills that are inculcated (table3).

Maybe the effort devoted to education relative to GDP was high and the country could not have afforded a bigger sacrifice. Nevertheless, the returns of the educational system were not high enough having been just average. The issue today is to spread education

much further, and more so, to educate better. This being more in conformity with the needs of development (Berryman 1991).

The allocation of resources among different levels and types of training remains a challenge for all countries. The optimal mechanisms seem hard to design, but, at least, there are obvious moves and adjustments that may be undertaken with low cost and high returns and that would lead to easier employment of skilled labor (since unemployment of skilled labor is a rising phenomenon).

An action plan is required to induce a critical mass of technological research, and the acceleration of the learning process with the expected spillover effects. Some procedure, combining market and government activities, is to be instituted in order to establish prompt coordination and cooperation between educational institutions, businesses and government.

The purpose being technical progress and hence competitiveness and growth, such an action plan may include as a major component the dissemination of work and business ethic, which constitute a basic ingredient for the improvement of the country's human resources and the resource allocation mechanisms.

This qualitative long term transformation of behavior and attitudes would generate the driving force for the favorable dynamic effects and the transition to a really modern economy.

Infrastructure and Services.:

There is a need for increased investments and for better allocation of such investment among sectors and between public and private sectors. There is a particular need for more massive investments in infrastructure and services to increase the quality of telephones, transportation, access to various sources of information and information networks, where a lot remains to be done (table 4). This is the kind of investment that will create the right environment for genuine development, but it is also the kind that raises the most difficult financial and informational problems.

Institutions and Incentives:

Development also requires more efficient institutions and regulations. The institutional reform, which is most urgently needed, would be to modernize government agencies and institutions. Centralized, multiple, complex and yet ineffective controls, vague and contradictory procedures and laws often characterize the behavior of administrative services in all fields. It is a priority to address this issue and to look for efficiency in the public sector, for example, through the introduction of rational (often private-like) organization. Given that the public sector is not to completely disappear because it is

necessary for the provision of public goods and for the regulation of externalities, administrative reform is very important.

The Environment:

Efficient administrative services are needed, in particular for environmental protection. Environmental issues are key issues and still badly in need of effective government regulation. Even though Tunisia was among the first to adopt an official environmental strategy, environment degradation and neglect are real and awareness is limited. A serious gap between plans and implementation exists. This issue is of course linked to the management of natural resources. Water, the most determinant and constraining resource suffers the most from pollution (World Bank 1995 b).

Tunisia is also rapidly depleting some of its key natural resources (which are in fact quite limited). It is already a net oil importer and it is expected to attain a much a higher oil deficit leading to a serious financial constraint. In approximately twenty years, Tunisia will probably have to import 90% of its oil consumption (around 20 million tons a year).

Yet huge investment is needed elsewhere. Will savings, domestic and foreign, then be available? Again it will depend on the attractiveness of the overall environment and on the credibility of government plans.

Credibility:

Reform implementation and the emergence of dynamic effects depend on the existence of a national consensus and on the acceptance of the national strategic objectives by a wide majority, which does not exclude conflicts that are a fact of life. In real life, there are conflicting interests and most transformations create losers and winners but stability may be reached through consensus. Otherwise there would be a credibility gap. In Tunisia, partners are yet to reach the needed consensus. Potential losers resist liberalization. Rent seekers are still powerful and are not interested in the promotion of an efficient, transparent and more civilized society.

This political economic issue is closely connected to that of democracy. The relationship between political stability, income distribution political freedom and the existence and the operation of democratic (or participate) institutions, and social values on the one hand and growth and development on the other hand, according to a recent analysis (Perotti 82), tend to indicate positive correlation. From this point of view, Tunisian rating is among the best in the region but it is again rather average compared to highly performing countries. An attractive environment, for human and financial capital, requires more than an average rating.

CONCLUSION

Therefore, a profound social transformation leading to higher productivity and generating the projected dynamic effects would be the result of more human capital accumulation, infrastructure, high quality services, a cleaner environment and more equitable and efficient institutions...

These requirements may seem unreachable. In fact they characterize all developed countries and it is obvious that in a developing country they cannot be gathered instantaneously. The main thing is to start a cumulative and convergent process but this is again a task of successful governance.

It is reasonable to conjecture that the creation of the FTA with the European Union and the whole liberalization program may well prompt such a modernization process which should lead to long term development. If the requirements are not fulfilled regress may be the alternative (sen 1993).

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**Table 1: Per Capita Income in Representative Countries
Relative to Tunisia in 1992**

	In \$ US	relative to Tunisia
Tunisie	1760	1
Morocco	1050	0.6
Turkey	2040	1.15
Romanie	1170	0.66
Poland	1950	1.1
China	480	0.27
Egypt	650	0.37

Source : The Word Bank

**Table 2: Export Earnings in Million Dinars
(at 1990 prices)**

1 TD = \$ 1 US approximately).

	1986	1990	1992	1994
- Petroleum	560	535	440	372
- Phosphate	416	454	463	432
- Agriculture and processed	248	348	427	341
- Textile and Leather	637	1179	1388	1683
- Mechanical and Electrical	159	302	366	462
- Tourism	483	828	948	1280
	<hr/>	<hr/>	<hr/>	<hr/>
- Total exports	3123	4592	5112	5516

Source: “ Budget Economique”: Ministry of Economic Development

**Table 3: Education Illiteracy and Women Employment in Tunisia
Compared to Some Selected Countries (%)**

	SCHOOL			Illiteracy	Women
	Primary	Secondary	Tertiary		Employed
TUNISIA	95	42	9	35	25
ALGERIA	88	60	12	43	10
MOROCCO	66	28	10	51	21
TURKEY	99	51	15	19	34
PORTUGAL	99	68	23	15	37
FRANCE	100	100	43	-	40

Source: World Bank “World Development Report 1994”.

**Table 4: General Infrastructure in Tunisia
Compared to Some Selected Countries**

COUNTRY	RAILROADS (KM/1000KM ²)	THGH WAYS (KM/MILLION PEOPLE)	TELEPH. LIN/1000 PEOPLE	ELECT.MILLION KWH/MILLION PEOPLE.
TUNISIA	14	2135	37	186
ALGERIA	2	1719	31	181
MOROCCO	4	1133	16	92
TURKEY	11	795	12	285
PORTUGAL	39	6105	24	746
FRANCE	63	13003	493	1814

Source : The World Bank "World Development Report 1994".

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